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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1980

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No.

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J. NAT and JENICE HAMRICK,

PETITIONERS

versus

COMMISSIONER OF INTERNAL REVENUE,

RESPONDENT

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Petition for a Writ of Certiorari to the United States Court of Appeals for the Fourth Circuit

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J. Nat Hamrick and
Jenice Hamrick, (Pro Se)

Hamrick & Hamrick
J. Nat Hamrick, Esq.
Counsel for Petitioners
P. O. Drawer 470
Rutherfordton,
North Carolina 28139

## QUESTIONS PRESENTED FOR REVIEW

1. Can a taxpayer be denied credit for the loss of a farm when:

She owned a 1/2 interest in a 936 acre farm and had no funds to buy seed, to buy fertilizer, to pay labor or purchase machinery, and when

The only way she could farm the land was to get a farm oriented corporation in which she held stock to farm it for her;

AND WHEN that corporation could not farm it for her without mortgaging the property to obtain the necessary funds to farm it,

AND WHEN after several bad crop years, the mortgage was foreclosed and the farm lost?

2. Can the tax court establish the value of taxpayer's 1/2 interest in the said property as of the year 1920 at $38,000.00,

WHEN the only people who were familiar with the land in 1920 testified as follows - Walter Frederick Marvin said it was worth at

least $250.00 an acre and another, Winchester Grahm, testified it was worth four times more than surrounding open land, and both based their opinions on the fact that it was a highly cultivated plantation with houses, barns, packing sheds, cotton gin, syrup mill, pecan orchard and a small school on the property,

AND WHEN the only expert witness for the government based his opinion on sales of unimproved open land and testified that he did not take into consideration the improvements, to wit, cotton gin, seed storage warehouse, grain storage warehouse, packing sheds, syrup mill, livestock barn, pecan orchard, asparagus packing house and barn and windmill?

## TABLE OF CONTENTS


| | Page |
|---|---|
| QUESTIONS PRESENTED FOR REVIEW | 1 |
| TABLE OF CONTENTS | i |
| TABLE OF AUTHORITIES | ii |
| GROUNDS UPON WHICH THE JURISDICTION OF THIS COURT IS INVOKED | 3 |
| STATEMENT OF THE CASE | 5 |
| ARGUMENT | 7 |
| CONCLUSION | 28 |
| APPENDIX | Separate Volume |
| CERTIFICATE OF SERVICE | 31 |

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## TABLE OF AUTHORITIES


| | Page |
|---|---|
| Fox v. Commissioner of Internal Revenue, 190 F.2d 101 (1951)..... | 3, 16 |
| Vincent C. Giblin v. Commissioner of Internal Revenue, 227 F.2d 692.... | 21 |
| Jefferson Patterson and Marvin Patterson v. United States, 459 F.2d 457..... | 3,9 |
| Mercer v. Commissioner of Internal Revenue, 356 F.2d 708..... | 3,10 |
| Schulumberger Technology Corporation v. United States, 443 F.2d 1115..... | 20,21 |
| Trent v. Commissioner of Internal Revenue, 291 F.2d 669..... | 19 |
| 28 U.S.C. 1254(1)..... | 3 |
| Title 26 U.S.C. Section 165 (a), (b) and (c), (1) and (2)..... | 4,8,9,16 |
| Title 26 U.S.C. Section 166 (a)(1), (d)(1)(2) (A) (B)..... | 4,18 |

GROUNDS UPON WHICH THE JURISDICTION OF THIS COURT IS INVOKED ARE:

This Court's opinion is in direct conflict with Jefferson Patterson and Marvin Patterson v. United States, 459 F.2d 487, and Mercer v. Commissioner of Internal Revenue, 376 F.2d 708 (1967) and Fox v. Commissioner of Internal Revenue, 190 F.2d 101 (1951).

(i) The date of the decision of the Tax Court was March 5, 1979, Docket No. 7250-75.

(ii) The date of the decision of the United States Court of Appeals for the Fourth Circuit was March 6, 1981 and is unpublished.

(iii) The statutory provision believed to confer on this Court's jurisdiction to review the judgment below by writ of certiorari is 28 U.S.C. 1254(1).

(f) The Constitutional provision and statutes which this case involves are:

Title 26, U.S.C. Section 165 § (a), (b), and (c) (1) (2).

Title 26, U.S.C. Section 166 § (a) (1) (d) (1), (2) (A) (B).

## STATEMENT OF THE CASE

Jenice Brown Hamrick owned a one half interest in a 936 acre farm. She had no funds with which to buy seeds, fertilizer, machinery or to pay labor (Appendix page 41-43 ). Nor was she capable of managing the farm herself (Appendix page 41-43).

In order to run the farming business and make a profit she agreed to execute a mortgage to secure a note of a family corporation, in exchange for that corporations agreement to advance all the necessary funds, furnish the labor and management, and operate the farm for her. The corporation had machinery, management, grain storage, and a cotton gin, and all things necessary to keep the farm in operation, and was run by her brother who owned the other one half interest in the 936 acre farm. (Appendix page 41-43 ).

Several bad farming years made it impossible to pay the mortgage and the mortgage was foreclosed and she lost her one half

interest in the farm, which she had pledged in order to try to operate the farm at a profit. (Appendix page 9 ).

She filed a joint return with her husband and deducted the loss. The Commissioner denied the deduction and the matter went to the Tax Court, which decided that the loss was a "non-business bad debt", and only dedeductible as a short term capital loss. The United States Court of Appeals for the 4th Circuit affirmed.

## ARGUMENT

Even if the taxpayers action in pledging the property for the corporation in exchange for the corporation's services and farming the land, resulted in some additional benefits to the corporation, such as greater utility of machinery and labor and the ginning of petitioners' cotton, this would not deprive her of the deduction because the primary motive for the mortgaging of her property was to secure funds to operate the farm at a profit.

She had no business other than the farm (Appendix page 42, 43). She had to run this farm the best way she could without any funds of her own. The only way she could run this farm was to get the corporation to do it for her, and the only way she could get the corporation to do it for her was to permit the place to be mortgaged in order for the corporation to obtain sufficient funds to farm it (Appendix page 42, 43). If she had been able to hire an overseer, borrow money to buy farm

machinery, seed, fertilizer, and then lost the place, it certainly would have been deductible.

Surely the fact that her financial condition was such that she could not operate the place herself through an overseer (she had only a one half interest) does not prevent her from deducting the real losses, which occurred because everyones effort to make a profit from the farm failed and the mortgage was foreclosed.

It now appears to petitioner that the loss was deductible under several sections of the Internal Revenue code.

TITLE 26, UNITED STATES CODE ANNOTATED SECTION 165 subsections (a), (b), (c), reads as follows:

"(a) General rule -- There shall be allowed as a deduction any loss sustained during the taxable year and not compensated for by insurance or otherwise.

(b) Amount of deduction -- For purposes of subsection (a), the basis for determining

the amount of the deduction for any loss shall be the adjusted basis provided in section 1011 for determining the loss from the sale or other disposition of property.

(c) Limitation on losses of individuals -- In the case of an individual, the deduction under subsection (a) shall be limited to --

(1) losses incurred in a trade or business;

(2) losses incurred in any transaction entered into for profit, though not connected with a trade or business;

Surely this loss was deductible under 165 (c) (1) and (2).

All the cases under this section hold that if the taxpayer engages in the transaction either in connection with a trade or business or with the intent to make a profit, the losses are deductible.

This proposition is supported by the following cases:

In the case of Jefferson Patterson and Marvin Patterson v. United States, 459 F.2d

487 is found the following language on page 494:

> "It might be concluded by exercise of hindsight that plaintiff did not operate Point Farm in the most efficient manner possible. However, it is not the quality of plaintiff's judgment in attempting to make Point Farm profitable that is controlling, but the fact that he made a good faith effort. Mercer v Commissioner of Internal Revenue, supra, 376 F.2d at 711; Lamont v. Commissioner of Internal Revenue, supra, 339 F.2d at 380; Doggett v. Burnet, supra, 65 F.2d at 194; Charles B. Pennington, supra, at 522."

Another which is extremely similar to this case is Mercer v. Commissioner of Internal Revenue, 376 F.2d 708(1967). In this case Petitioner Loy D. Mercer and his older brother Berle Mercer were raised on a cattle ranch in Nebraska. Berle moved to Alaska with his family and a herd of cattle. He acquired a

ranch in the interior of Alaska and began attempting to ranch for profit. His brother Loy moved to Alaska a year or so later, where he continued his college education, and before moving he owned some Angus cattle and traded them for six Angus-Highland cattle, which would survive better in the Alaska climate.

Loy tried twice to get a homestead and couldn't do it. He had no place to keep his cattle. He paid Berle $5,500 one year and $3,500 another year for taking care of his cattle. He sought to deduct this and the Commissioner disallowed it.

In the instant case, petitioner, Jenice Hamrick had a half interest in a farm. She had no way to farm it, she tried to get some way to farm it. The only way she could farm it was to get a corporation, that she and her brother both owned stock in, to use their machinery and farm the place, and in order to do this she had to pledge the place to get the necessary money to farm it.

She was in essentially the same position

as Loy D. Mercer, because she could not do anything with her farm except get the corporation to farm it, and he couldn't do anything with his cattle, except get his brother to keep them. She pledged all the property she had to get her place farmed, and he paid all the money he had to get his brother to look after his cattle.

The discussion of the matter by the Court, on page 710 and 711, is directly in point in this case:

> "It seems clear from a reading of the opinion of the Tax Court that its decision was in essence a conclusion that the taxpayer's venture was not aimed at profit because a reasonable man would not expect a profit from such a venture, and that while he might in future get into such a business, he had not yet done so in the years in question. We are aware that other circuits have insisted that the taxpayer's expectation of profit be both reasonable and in

good faith. See, e.g., Godfrey v. Commissioner of Internal Revenue, 335 F. 2d 82, 84 (6th Cir. 1964), Whitman v. United States, 245 F. Supp. 845 (W.D. La. 1965). Unquestionably, however, in this circuit the rule is that a taxpayer's venture is a trade or business if he has a good faith expectation of profit from that venture, irrespective of whether or not others might view that expectation as reasonable. Hirsch v. Commissioner of Internal Revenue, supra, 315 F.2d at 736, Brooks v. Commissioner of Internal Revenue, supra. We are not alone in this view. See, e.g., Lamont v. Commissioner of Internal Revenue, supra, 339 F.2d at 380, DuPont v. United States, 234 F. Supp. 681 (D.Del.1964). Here the taxpayer entered into a venture with a good faith expectation of profit. Whether that expectation was foolhardy or shrewd is of no moment. The taxpayer expended his effort and capital to the

limit of his available time and resources. There can be no conclusion other than that the taxpayer's venture, though small in results, was a trade or business within the meaning of sections 162 and 165." (Emphasis added)

In petitioners' case there was absolutely no reason except a desire to operate a business and make a profit, no sporting considerations were involved and petitioners took the only course available to them to farm their land. This is shown by the testimony of petitioner, J. Nat Hamrick, which appears on page 41-43 of the Appendix and reads as follows:

"Q During the three years in issue, 1970, 1971 and 1972, did either you or Mrs. Hamrick receive any rental income from Simon Brown's Sons, Incorporated, for the use of the Crum place?

A No, sir. The only thing that we received were pecans and food and things like that. There was not enough money

realized anywhere to pay us any income. The whole thing was in jeopardy at that time.

MR. BATES: No further questions, Your Honor.

THE COURT: All right. You may step down as a witness, Mr. Hamrick. Thank you.

THE WITNESS: Thank you, sir. I might say one other thing, if I can.

THE COURT: All right.

THE WITNESS: I had no alternative -- when my wife's mother gave her the Crum place, I was not able to farm it. I was practicing law and I had no surplus funds to farm it; I couldn't farm it. I had no way to farm it. She only had a half interest. So I -- there was nothing we could do except let Simon Brown's Sons farm it and if there was any surplus money, she could get it; and there was nothing that we could do except pledge the property for Simon Brown's Sons, cause it was a valuable

> piece of property and without it Simon Brown's Sons couldn't run. I had no way to farm it. I couldn't buy the seed, I couldn't buy the fertilizer, I couldn't do anything with it. So to get any income out of it at all, or get the hope of future income, all I could do was say to my brother-in-law that's running Simon Brown's Sons, "All right, we'll pledge the place for you. You run it and maybe we'll get some income out of it in the future." That's all I could do. . . . You're borrowing from hand to mouth and Peter to pay Paul to get seeds and fertilizer and stuff. That's the reason it was done that way."

Another case which strongly supports petitioners position is Fox v. Commissioner of Internal Revenue, 190 F.2d 101 (1951).

This loss was also deductible under Title 26, United States Code Annotated Section 165 (c) (1), as a loss incurred in a trade or business.

The position of the Commissioner of Internal Revenue that this was a "nonbusiness bad debt", is not in accord with the facts. If a farm is not kept in production, no one can make a profit on it. It grows up, weeds take over, taxes accumulate, and in just a few years it will be totally useless and can be restored only by substantial capital expenditures. In order to keep a farming business profitable, the farm must stay in production. Surely her efforts to keep this farm in operation, so a profit could be made on it was a business endeavor, and her losses were occasioned by the bad crop years which caused her business to fail.

Petitioners' Appellants do not understand how the Commissioner could have characterized this loss as a "nonbusiness bad debt". The corporation did not owe petitioners anything. The debt was owed by the corporation to the lending agency and the petitioners pledged their property to guarantee the payment of the corporation debt so

it could obtain funds to farm the property. When the farm could not make the money to pay the debt, foreclosure was instituted and the farm sold.

Under Title 26, United States Code Annotated Section 166 (a) (1) Wholly worthless debts we find the following:

"(a) General rule --

(1) Wholly worthless debts -- There shall be allowed as a deduction any debt which becomes worthless within the taxable year."

Under Section 166 (d)(2) Nonbusiness debt defined, we find the following:

"(2) Nonbusiness debt defined -- For purposes of paragraph (1), the term "nonbusiness debt" means a debt other than --

(A) a debt created or acquired (as the case may be) in connection with a trade or business of the taxpayer; or

(B) a debt the loss from the worthlessness of which is incurred in

the taxpayer's trade or business."

Surely under these paragraphs, petitioners loss was a business bad debt when they had no reason to incur the debt, except to operate the farm - taxpayer's only business - and no way to operate the farm, except to incur the debt. (Appendix page 41-43 ).

This action is supported by the following cases:

Trent v. Commissioner of Internal Revenue, 291 F.2d 669 (1961), is directly in point where Headnote 2 reads as follows:

> "Employee, who made loans to corporate employer in order to hold his job, could deduct for a business bad debt when loans became worthless. 26 U.S. C.A. (I.R.C.1954) § 166 (d) (2) (A)."

And Justice Friendly states on page 676:

> "Where, as here, it is plain that the loans were made in connection with the taxpayer's "trade or business or rendering services for pay," Folker v.

Johnson, supra, 230 F.2d at page 909, the statutory requirement has been met.

Judgment reversed."

In the case of Schlumberger Technology Corp. v. U.S.A., 443 F.2d 1115, Judge Thornberry, Judge Wisdom and Judge Dier held that the loans in question were proximately related and had a dominate business motivation even though they only related to a secondary part of the taxpayer's business. It is said on page 1122:

"Although the Taxpayer's primary business was measuring physical phenomeonon in the earth for aid in detecting minerals, it also engaged in developing telementary devices and related measurement components for use by military and space agencies. . . . When it became clear that the personnel were not providing the research and knowledge needed by the taxpayer, taxpayer sold ASI. In these circumstances, it is evident that

the ASI transactions were intrigal and necessary acts in the conduct of SWSC's business and were made with a business and not an investment motive. It follows that the ASI stock and debts were not capital assets and that taxpayer's losses were not covered by Section 1232. For the reasons as stated above, the judgment of the District Court is affirmed as dealing with that portion of the judgment dealing with taxpayer's loss on the CSI notes."

To the same effect is Vincent C. Giblin, v. Commissioner of Internal Revenue, 227 F.2d 692. The relevant holding in this case is set forth in Headnote 2, which reads as follows:

"Where a taxpayer, on 11 or 12 occasions between 1926 and 1945, had contributed time, talent, energy and money to exportation of ideas to make money a part from his law practice, lending such aid to these enterprises as he considered

would best accomplish that purpose, he was engaged in the business of dealing in enterprises, and a loss suffered from worthlessness of a loan made to one of these enterprises was deductible in full as a bad business debt."

To the same effect is Mears v. Commissioner of Internal Revenue, 272 F.2d 788. It cites with approval U.S. Tax Court in Dorminey v. Commissioner, 26 Tax Court 940 (August 1956). Here the petitioner made a loan to United States and Panama Navigation Company in which he was an officer and stockholder. The loan was made to insure a steady supply of bananas. Petitioner's economic motive in making the loans was to further his principal business of food distribution. The Tax Court held that the loans, which later became worthless, "were so incidental and proximately related to his true business that the taxpayer was allowed to deduct the amount of the loans as business bad debts." . . . "The Tax Court said, "Whether or not the

petitioner, by his financing activities, was engaged in the money lending business may not be determined since the bad debt loss was incidental to and proximately related to his produce business.'"

We now come to the question of the value of the Crum Place Farm in the year 1920, when it was given to Zelma Brown. At the hearing in Winston-Salem, North Carolina, the Government's witness, Mr. Cox testified that he had investigated the matter and gave his opinion as to the value of the land at that time by looking at comparables as shown by the records which allegedly represented what land was sold for during that period. In his testimony he recited the fact that he did not contact anyone who was living at the time and who had personal knowledge of the matter (Appendix page 32, 33). He testified that he considered only the value of the land itself with no improvements (Appendix page 32). Mr. Cox testified that if it appeared that the property contained a cotton gin, a seed storage

warehouse, 10 dwelling, cotton seed storage warehouse and a grain storage warehouse, it would change the value of the property and he would be valuing a business and not bare farmland (Appendix page 34 ). He said that if he had been called on to evaluate the property in 1920, he would have taken into consideration the value of all the improvements, (Appendix page 34 ) and further testifying that this was a very good cotton plantation. (Appendix page 33 ).

In his testimony, Stanley Brown stated that in 1920 he was a student at the University of Virginia (Appendix page 35, 36) and was 16 years old and worked for his father. That he assisted in the supervision of the Crum Place Farm and that he was familiar with the improvements on the property (Appendix page 35, 36). That at that time, there was a large overseer's house, containing six or seven bedrooms, bathroom facilities; that there was a windmill, a large barn and yard where mules and livestock were kept, a cow

barn, a syrup mill and a cotton gin; that there was a deep well for water and a telephone line that they had constructed themselves for a distance of six miles. (Appendix page 35, 36). That it had an asparagus packing house and a large pecan orchard. (Appendix page 37 ). That it had storage facilities for cotton seed and all other farm products on the place. (Appendix page 38 ) That this plantation was unique in that in that area of South Carolina many times a farm would have large amounts of bad land and large amounts of good land. That the Crum Place Farm had very little of what was called bone, land that was unproductive and tha there was not more than 12 acres of bone, unproductive land. (Appendix page 39, 40). That it had between 75 and 90 acres of asparagus, which meant that the crowns were down in the land and were harvested every year. That the property had its own asparagus packing house. That some of this land was black cucumber bottom land, consisting of

about 100 acres, which was very productive and that also located on the property was a cucumber packing shed. (Appendix page 38 ).

In the deposition of Winchester Graham, who was deposed on September 29, 1977, in Columbia, South Carolina, he stated that he was living in Denmark, South Carolina, about six miles from the Crum Place Farm in 1920. (Appendix page 29 ). That he was familiar with the property and that it had a cotton gin and grain storage and dwellings on it. (Appendix page 29 ). That this property and the Guess property was the best property in that part of the State. (Appendix page 29 ). He stated on page 5 of the record that he valued this property against ordinary open land in that part of South Carolina to be four times what the ordinary land would be valued at, and specifically stated as follows:

> "Q Now, suppose that this other land that was sold there is open land with good fertile land, how much more would

you say that this working plantation with everything on it would be worth?

A Well, I'd rather take it on a percentage. I'd say, if you have a dollar over here, you'd get about four dollars over here (Indicating) per acre. I'd say about four to one, but I'm taking the poorest part of Barnwell County against the better part of Barnwell County.

Q Now, if Mr. Bates has sales somewhere in this area for open land that was bringing sixty to eighty dollars an acre and my father-in-law had a complete working plantation with cotton gin and everything on it, how much more would you say that it would be worth than the other?

A I'd say at least three or four times." (Appendix page 28 ).

Further on page 6 upon cross examination, Mr. Graham testified that he was 24 years old in 1920 and that he did not know of any land

in the area as good as the Crum Place Farm, except the Guess property located about four or five miles away. (Appendix page 29 ).

Mr. Walter Frederick Marvin was deposed on September 29, 1977, as to value and stated that he was 85 years old; that he remembered in the '20's that the Crum Place Farm had tenant houses and a cotton gin. (Appendix page 30 ). He testified on page 2 of the record that from his opinion of land being traded in the area, he felt that the Crum Place Farm was worth at least $250.00 an acre because the land was extremely fertile and in good shape and that the Crum Place Farm and the Guess property were the two most valuable places in the area. (Appendix page 30 ).

## CONCLUSION

In conclusion, petitioners respectfully submit that the mortgaging of the land for Simon Brown's Sons was dominately motivated by business considerations - was entered into

for profit - and it was the only thing petitioners could do to operate the Crum Place Farm and was deductible from income under the code sections referred to herein.

Petitioners also contend that the operation of the Crum Place Farm was the only business of Jenice B. Hamrick and that she could not operate it except through Simon Brown's Sons and Simon Brown's Sons could not finance the operation without the funds raised by mortgaging the Crum Place Farm and, therefore, the mortgage and loss of the property was for business reasons and a business bad debt loss.

That the fair market value of the Crum Place farm as of December 20, 1920, which is the basis year, was at least $250.00 an acre and that Taxpayers' loss was at least $125,000.00.

Respectfully submitted, this the _____ day of June, 1981.

J. Nat Hamrick

Jenice B. Hamrick

PETITIONERS

Hamrick & Hamrick
P. O. Drawer 470
Rutherfordton, NC 28139
Counsel for Petitioners

CERTIFICATE OF SERVICE

This is to certify that the undersigned, a member of the bar of this Court, served this Petition for a Writ of Certiorari and Appendix thereto upon all the parties to this action by depositing at least three copies of the Petition and three copies of the Appendix in the United States mail addressed to the attorneys whose names and post office address are:

M. Carr Ferguson, Asst. Attorney General
Gilbert E. Andrews
Jonathan S. Cohen
Jay W. Miller, Attorneys
Tax Division, Department of Justice
Washington, D.C. 20530

This 2 day of June, 1981.

J. Nat Hamrick
Hamrick & Hamrick
P. O. Drawer 470
Rutherfordton, N.C. 28139
(704)287-3359